

No. 14090

United States
Court of Appeals
for the Ninth Circuit

HELGA CARLEN, JOHN T. CARLEN, CATH-
RYN McKAY, ARTHUR R. McKAY, AR-
THUR R. and CATHRYN McKAY and
JOHN T. and HELGA CARLEN,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of Record

Petition to Review a Decision of The Tax Court
of the United States

FILED

MAR 10 1954

PAUL P. O'BRIEN
CLERK

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McKAY, ARTHUR R. McKAY, ARTHUR R.
and CATHRYN McKAY and
JOHN T. and HELGA CARLEN,

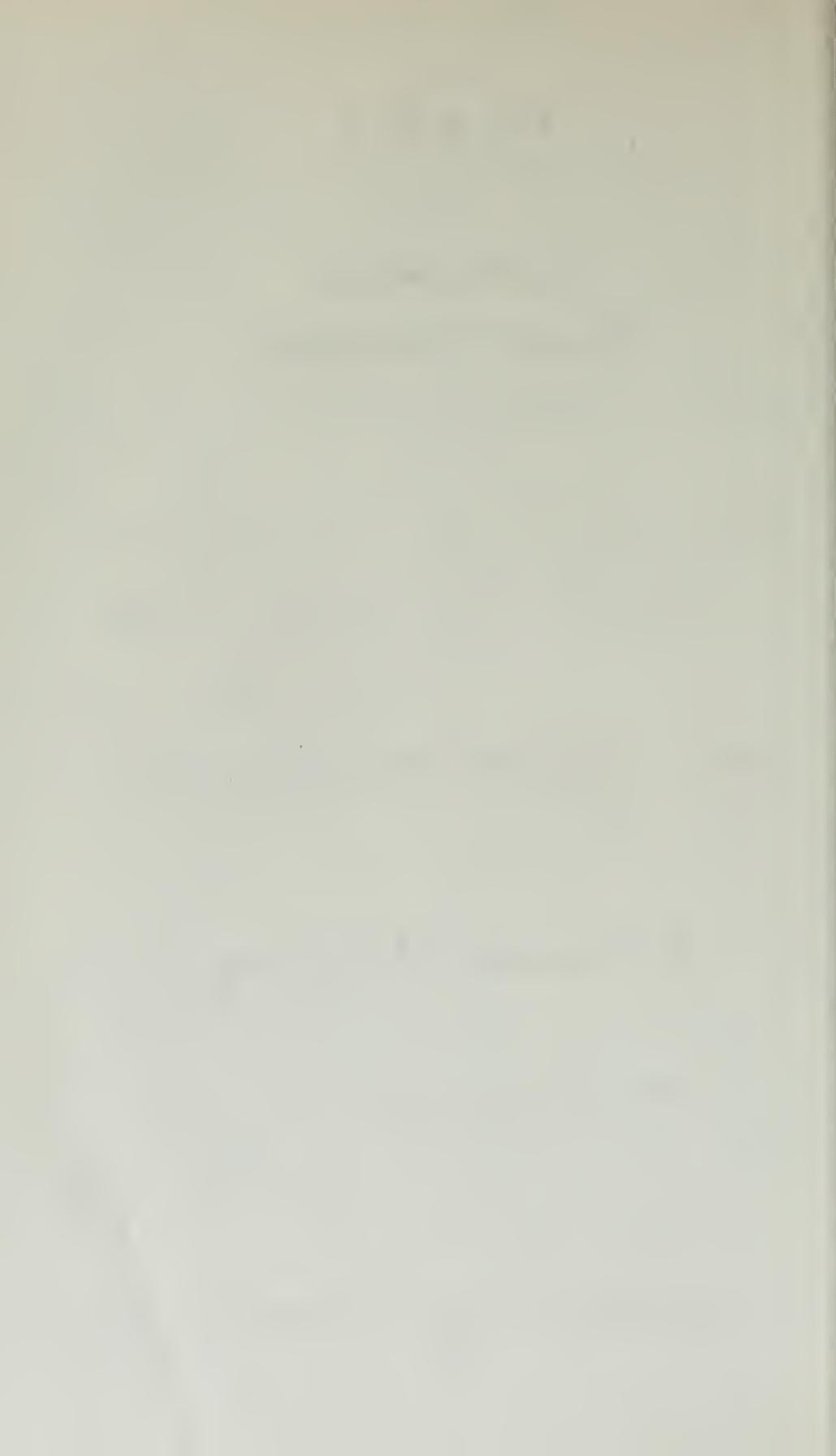
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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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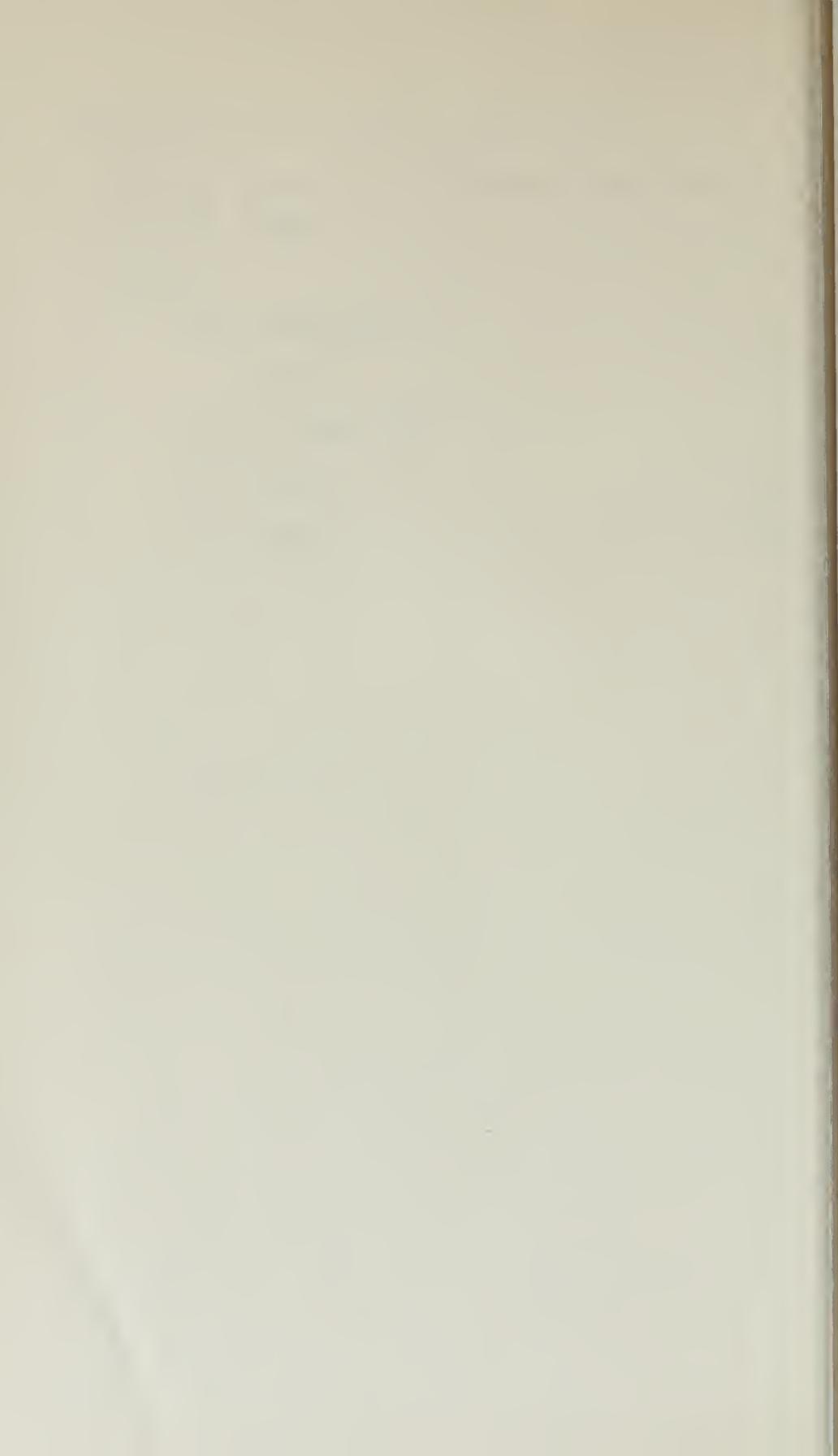
Aiken, Robert L.

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—cross 53



APPEARANCES:

For Petitioners:

CHARLES F. OSBORN, Esq.
GEORGE F. KACHLEIN, Esq.,

For Respondent:

JOHN J. WELCH, Esq.

DOCKET ENTRIES

1952

- June 17—Petition received and filed. Taxpayer notified. Fee paid.
- June 20—Copy of petition served on General Counsel.
- June 17—Request for Circuit hearing in Seattle, Washington, filed by taxpayer. 6/26/52—Granted.
- Aug. 5—Answer filed by General Counsel.
- Aug. 5—Request for Hearing in Seattle, Wash., filed by General Counsel.
- Aug. 14—Copy of answer and request served on taxpayer, Seattle, Wash.
- Oct. 8—Hearing had before Judge Tietjens on merits. Petitioner's motion to consolidate 37662 thru 37665 and add 42122 and 42123, concurred in by respondent, granted. Consolidated, and dockets 42122 and 42123 added and assigned to Seattle calendar of October 6, 1952. Stipulation of Facts with Exhibits 1 thru 10 and A thru N, filed. Briefs Dec. 8, 1952; Replies Jan. 7, 1953.

1952

Oct. 22—Transcript of Hearing 10/8/52 filed.

Dec. 8—Brief filed by taxpayer. Copy served 2/3/53.

Dec. 8—Motion for extension to 12/29/52 to file brief, filed by General Counsel. 12/9/52—Granted.

Dec. 29—Motion for extension to 1/31/53 to file brief, filed by General Counsel. 12/31/52—Granted.

1953

Feb. 2—Brief filed by General Counsel.

Mar. 2—Reply Brief filed by General Counsel.

Mar. 4—Reply Brief filed by taxpayer. Copy served 3/5/53.

May 29—Findings of Fact and Opinion rendered. Judge Tietjens. Decision will be entered under Rule 50. 6/2/53—Served.

June 23—Agreement by parties for entry of decision filed.

June 25—Decision entered. Judge Tietjens. Div. 1.

Sept. 17—Petition for review by U. S. Court of Appeals for the Ninth Circuit with assignments of error and acknowledgment of service thereon filed by taxpayer.

Sept. 17—Proof of Service filed by taxpayer.

Sept. 17—Designation of contents of record filed by taxpayer with proof of service thereon.

The Tax Court of the United States

Docket No. 42123

JOHN T. CARLEN and HELGA CARLEN, hus-
band and wife, Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION

The above named petitioners hereby petition for a redetermination of the deficiency in income tax as set forth by the Commissioner of Internal Revenue in his notice of deficiency (Symbols: Seattle Division, Internal Revenue Service, IT:90D:TRB) dated March 21, 1952 and as the basis of this proceeding allege as follows:

1. The petitioners are husband and wife with residence at 504 12th Street, Raymond, Washington. The income tax returns for the calendar years 1948, 1949 and 1950 here involved were filed with the Collector for the District of Tacoma.

2. A notice of deficiency (a copy of which is attached and marked Exhibit "A") was mailed to petitioners under date of March 21, 1952.

3. The tax controversy is income tax for the calendar years 1948, 1949 and 1950 in the amounts of \$3,904.26, \$3,093.50 and \$1,401.90, respectively.

4. The determination of tax set forth in said notice of deficiency is based upon the following error:

That petitioners, as members of the partnership of McKay and Carlen, were not entitled

to report the gain received from the sale of certain timber under the provisions of Section 117(k) of the Internal Revenue Code, but that all of the gain is to be taxed as ordinary income.

5. The facts upon which petitioners rely as the basis of this proceeding are as follows:

(a) Petitioners are members of a partnership, McKay and Carlen; that said partnership during the taxable years in question was engaged in the logging business in a proprietary capacity.

(b) McKay and Carlen entered into a contract with the Neuskah Tbr. Co., Inc., under date of April 21, 1945, to log and to acquire certain species of timber in a certain area and to pay therefor a certain stumpage after which payment all proceeds of sale belonged to McKay and Carlen; that said contract was subsequently orally amended to include hemlock; that after the dissolution of Neuskah Tbr. Co., Inc. the partnership continued the logging operations under oral contract with E. K. Bishop Lumber Company, successor to Neuskah Tbr. Co.

(c) That said contracts were in existence for a period of more than six (6) months prior to the beginning of the taxable years in question.

(d) That the partnership had a full economic interest in and to the timber cut and converted into logs and then sold under the Neuskah and Bishop contracts as the partnership took the full risk of gain or loss on the cutting, and marketing of such timber; that the partnership bore all of the logging

expense without right of reimbursement from the original timber owner.

(e) That the partnership was not logging under a "service contract" but had a contract right to cut and acquire the timber in question.

(f) The taxpayers and the partnership, McKay and Carlen, properly elected in their tax returns to report the gain realized on the timber and logging operation in question, as long-term capital gain in accordance with Section 117(k) of the Internal Revenue Code.

(g) The partnership of McKay and Carlen was engaged in the business of cutting timber on contract for its own profit in the taxable years in question.

Wherefore, petitioners pray that this Court may hear the proceeding and determine:

(a) That the petitioners are not liable for any additional income tax for the taxable years 1948, 1949 and 1950 by reason of the gain realized on the sale of timber.

(b) That the petitioners, as members of the partnership of McKay and Carlen, properly returned their share of the profits realized by the partnership on the cutting and sale of timber as long-term capital gain taxable under Section 117(k) of the Internal Revenue Code.

(c) That the petitioners as members of the partnership of McKay and Carlen were engaged in the acquisition, cutting and sale of timber in the taxable years involved in accordance with contracts in

existence for more than six months prior to the beginning of each taxable year.

(d) That the Court give these petitioners such other and further relief as is just and equitable in the premises.

/s/ CHARLES F. OSBORN,
/s/ GEORGE F. KACHLEIN, JR.,
Counsel for Petitioners

Duly Verified.

EXHIBIT "A"

Form 1230-A (1951) Internal Revenue Service

U. S. Treasury Department

Office of Internal Revenue Agent in Charge

Securities Bldg., Seattle 1, Washington

IT:90D:TRB

March 21, 1952

Mr. John T. Carlen and Mrs. Helga Carlen

Husband and Wife

504 12th Street, Raymond, Washington

Dear Mr. and Mrs. Carlen:

You are advised that the determination of your income tax liability for the taxable years ended December 31, 1948, 1949 and 1950, discloses a deficiency of \$8,399.66, as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days from the date of the mailing of this letter you may file a petition with The Tax Court of the United States, at its principal address, Washington 4, D. C., for a redetermination of the deficiency. In counting the 90 days you may not exclude any day unless the 90th day is a Saturday, Sunday, or legal holiday in the District of Columbia, in which event that day is not counted as the 90th day. Otherwise Saturdays, Sundays, and legal holidays are to be counted in computing the 90-day period.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to this office for the attention of TRB:90D. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after receipt of the form, or on the date of assessment, or on the date of payment, whichever is earlier.

Very truly yours,

JOHN B. DUNLAP,

Commissioner,

/s/ By S. R. STOCKTON,

Internal Revenue Agent in Charge

Enclosures: Statement, Form 1276, Agreement
Form 870.

TRB:em

Statement

Income tax liability for the taxable years ended December 31, 1948, 1949, and 1950.

Year	Deficiency
1948	\$3,904.26
1949	3,093.50
1950	1,401.90
	<hr/>
Total.....	\$8,399.66

In making this determination of your income tax liability, careful consideration has been given to the report of examination dated October 18, 1951 and to your protest dated January 19, 1952.

A copy of this letter and statement has been mailed to your representative, Mr. Robert L. Aiken, 535 Finch Building, Aberdeen, Washington, in accordance with the authority contained in the power of attorney executed by you.

Taxable year ended December 31, 1948

ADJUSTMENTS TO NET INCOME

Net income as disclosed by return, Form 1040.....	\$ 18,430.64
Unallowable deductions and additional income:	
(a) Partnership income	23,227.36
	<hr/>
Total.....	\$ 41,658.00
Nontaxable income and additional deductions:	
(b) Capital gains	11,613.68
	<hr/>
Net income as adjusted.....	\$ 30,044.32

EXPLANATION OF ADJUSTMENTS

(a) It has been determined that your distributable share of ordinary net income of the partnership, McKay and Carlen, for the

APPEARANCES:

fiscal year ended April 30, 1948 was \$32,377.60 whereas you have reported income of \$9,150.24 from that source. Net income is therefore increased by \$23,227.36, the difference between the above two amounts.

(b) On your return you reported capital gain of \$11,645.67 whereas your corrected income from that source has been determined to be \$31.99, a difference of \$11,613.68. Net income is reduced accordingly.

COMPUTATION OF TAX

Net income as adjusted	\$30,044.32	
Less: Exemptions	2,400.00	
		<hr/>
Income subject to tentative tax.....	\$27,644.32	
One-half of income subject to tentative tax.....	\$13,822.16	
Tentative tax		\$ 4,183.53
Tax reduction:		
17 per cent of \$400.00.....	\$ 68.00	
12 per cent of \$3,783.53.....	454.02	522.02
		<hr/>
Balance		\$ 3,661.51
Tax liability (\$3,661.51 x 2).....	\$ 7,323.02	
Tax liability per return—Account No.		
9120185	3,418.76	
		<hr/>
Deficiency of income tax.....		\$ 3,904.26

Taxable year ended December 31, 1949

ADJUSTMENTS TO NET INCOME

Net income as disclosed by return, Form 1040.....	\$21,019.06
Unallowable deductions and additional income:	
(a) Partnership income	17,858.76
	<hr/>
Total.....	\$38,877.82
Nontaxable income and additional deductions:	
(b) Capital gains	8,929.38
	<hr/>
Net income as adjusted.....	\$29,948.44

EXPLANATION OF ADJUSTMENTS

(a) It has been determined that your distributable share of or-

dinary net income of the partnership. McKay and Carlen, for the fiscal year ended April 30, 1949 was \$30,868.13 whereas you have reported income of \$13,009.37 from that source. Net income is therefore increased by \$17,858.76, the difference between the above two amounts.

(b) On your return you reported capital gain of \$9,589.38 whereas your corrected income from that source has been determined to be \$660.00, a difference of \$8,929.38. Net income is reduced accordingly.

COMPUTATION OF TAX

Net income as adjusted.....	\$29,948.44	
Less: Exemptions	2,400.00	
	<hr/>	
Income subject to tentative tax.....	\$27,548.44	
One-half of income subject to tentative tax..	\$13,774.22	
Tentative tax		\$ 4,162.91
Tax reduction:		
17 per cent of \$400.00.....	\$ 68.00	
12 per cent of \$3,762.91.....	451.55	519.55
	<hr/>	<hr/>
Balance		\$ 3,643.36
Tax liability (\$3,643.36 x 2).....	\$ 7,286.72	
Tax liability as disclosed by return—		
Account No. 3029871	4,193.22	
	<hr/>	<hr/>
Deficiency of income tax.....		\$ 3,093.50

Taxable year ended December 31, 1950

ADJUSTMENTS TO NET INCOME

Net income as disclosed by return, Form 1040.....	\$ 5,804.23	
Unallowable deductions and additional income:		
(a) Partnership income	13,781.77	
	<hr/>	<hr/>
Total.....	\$19,586.00	
Nontaxable income and additional deductions:		
(b) Capital gain	\$ 6,886.72	
(c) Standard deduction	355.08	7,241.80
	<hr/>	<hr/>
Net income as adjusted.....		\$12,344.20

EXPLANATION OF ADJUSTMENTS

(a) It has been determined that your distributable share of ordinary net income of the partnership, McKay and Carlen, for the fiscal year ended April 30, 1950 was \$14,130.03 whereas you have reported income of \$348.26 from that source. Net income is therefore increased by \$13,781.77, the difference between the above two amounts.

(b) On your return you reported capital gain of \$6,886.72 whereas it has been determined that you had no income from that source. Net income is reduced accordingly.

(c) On your return you claimed a standard deduction of \$644.92. It has been determined that a standard deduction of \$1,000.00 is allowable. Accordingly, net income is reduced by \$355.08, the difference between the above two amounts.

COMPUTATION OF TAX

Net income as adjusted.....	\$12,861.49	
Less: Exemptions	2,400.00	
		<hr/>
Income subject to tentative tax.....	\$10,461.49	
One-half of income subject to tentative tax..	\$ 5,230.75	
Tentative tax		\$ 1,160.00
Tax reduction:		
13 per cent of \$400.00.....	\$ 52.00	
9 per cent of \$760.00.....	68.40	120.40
		<hr/>
Balance		\$ 1,039.60
Tax liability (\$1,039.60 x 2).....	\$ 2,079.20
Income tax liability as disclosed by return—		
Account No. 8067165	673.34
		<hr/>
Deficiency of income tax.....		\$ 1,405.86

[Endorsed]: T.C.U.S. Filed June 17, 1952.

[Title of Tax Court and Cause No. 42123.]

ANSWER

Comes now the Commissioner of Internal Revenue, by his attorney, Charles W. Davis, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition herein, admits and denies as follows:

1. Admits the allegations contained in paragraph 1 of the petition.

2. Admits the allegations contained in paragraph 2 of the petition.

3. Admits the allegations contained in paragraph 3 of the petition.

4. Denies that the Commissioner erred in determining the deficiency as set forth in the notice of deficiency from which petitioners' appeal is taken. Specifically denies the Commissioner erred as alleged in paragraph 4 of the petition.

5. (a) Admits the allegations contained in subparagraph (a) of paragraph 5 of the petition.

(b) Admits that McKay and Carlen entered into a contract with the Neuskah Tbr. Co., Inc., under date of April 21, 1945, to log timber in a certain area. Denies the remaining allegations contained in subparagraph (b) of paragraph 5 of the petition.

(c) to (g), inclusive. Denies the allegations contained in subparagraphs (c) to (g), inclusive, of paragraph 5 of the petition.

6. Denies generally and specifically each and every material allegation contained in the petition, not hereinbefore specifically admitted, qualified or denied.

Wherefore, it is prayed that the petitioners' appeal be denied and that the Commissioner's determination of deficiency be approved.

/s/ CHARLES W. DAVIS,
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:

WILFORD H. PAYNE,
District Counsel,

DOUGLAS L. BARNES,
JOHN H. WELCH,
Special Attorneys, Bureau of Internal
Revenue.

[Endorsed]: T.C.U.S. Filed Aug. 5, 1952.

20 T. C. No. 77

The Tax Court of the United States

Docket Nos. 37662, 37663, 37664, 37665, 42122, 42123

HELGA CARLEN, et al., Petitioners,*

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Promulgated May 29, 1953.

FINDINGS OF FACT AND OPINION

Capital Gains and Losses—Timber Cutting—Section 117 (k) (1), Internal Revenue Code.

A partnership in which the taxpayers had an interest entered into contracts for logging timber on lands owned by others. For this service they were to be paid compensation measured by the difference between market price of the timber cut and specified stumpage plus a "service fee". Held, the taxpayers were not entitled to capital gains treatment on the timber cut under Section 117 (k) (1).

Charles F. Osborn, Esq., for the petitioners.

John H. Welch, Esq., for the respondent.

* Proceedings of the following petitioners are consolidated herewith: John T. Carlen; Cathryn McKay; Arthur R. McKay; Arthur R. McKay and Cathryn McKay, husband and wife; and John T. Carlen and Helga Carlen, husband and wife.

The Commissioner determined the following deficiencies in income tax:

Year	Taxpayer	Amount
1947	Arthur R. McKay.....	\$ 561.52
1947	Cathryn McKay	561.52
1947	John T. Carlen	548.01
1947	Helga Carlen	548.00
1948	Arthur R. and Cathryn McKay.....	3,928.78
1948	John T. and Helga Carlen.....	3,904.26
1949	Arthur R. and Cathryn McKay.....	3,052.04*
1949	John T. and Helga Carlen.....	3,093.50
1950	Arthur R. and Cathryn McKay.....	1,405.86
1950	John T. and Helga Carlen.....	1,401.90

* The stipulation of facts shows \$3,071.61 with no explanation for the difference.

The only issue is whether the Commissioner erred in finding that the taxpayers are not entitled to capital gains treatment of lumber cut under certain contracts as provided for in section 117 (k) (1) of the Internal Revenue Code.

Findings of Fact.

The stipulated facts are so found and the stipulation is included herein by reference.

Arthur R. McKay and Cathryn McKay are residents of Aberdeen, Washington. John T. Carlen and Helga Carlen are residents of Raymond, Washington.

For the calendar year 1947 the McKays and the Carlens, as members of marital communities, each filed a separate income tax return. For the calendar years 1948, 1949, and 1950 joint returns were filed. All returns were filed with the collector of internal revenue, Tacoma, Washington.

As of May 1, 1945, Arthur R. McKay and John T. Carlen formed an oral general partnership to engage in the logging and cutting of timber in Southwest Washington. During all the years in question the partnership was engaged in the trade or business of logging timber and was not engaged in the business of cutting timber for sale on its own account or for use in its business.

On March 15, 1945, Rayonier Incorporated and Neuskah Timber Company entered into a contract by the terms of which Neuskah purchased from Rayonier all of the merchantable cedar and spruce timber and certain hemlock located on tracts described in the contract and owned by Rayonier. Title to the timber and risk of loss by fire or other casualty was to pass to Neuskah on cutting. Rayonier was to designate the hemlock to be cut and all logs were to be branded with a distinctive design approved by Rayonier. Neuskah agreed to sell back to Rayonier and Rayonier agreed to buy all hemlock logs cut under the contract.

On April 23, 1945, Neuskah entered into the following contract with the McKay and Carlen partnership for cutting part of the spruce and cedar included in the Rayonier-Neuskah contract.

This contract, made and entered into by and between the Neuskah Tbr. Co. Inc., a corporation, of Aberdeen, Washington, hereinafter called First Party and Arthur R. McKay and John Carlen, of Aberdeen, Washington, a co-partnership, hereinafter known as McKay & Carlen, and hereinafter called Second Party, Witnesseth:

That First party owns or controls certain timber in Section Thirty (30) and North Half (N $\frac{1}{2}$) of Section Twenty-Nine (20), Township Thirteen (13) North, Range Nine (9) West, W.M., Pacific County, Washington.

Second Party agrees to selective log all the merchantable Sitka Spruce and Western Red Cedar on the above described land in accordance with the usual custom. In the conduct of said operation the Second Party agrees to comply with and conform to all the requirements of law now or hereafter during the term of the contract in effect relating to the operation of cutting, logging and removal of timber, or to fire or the prevention of fire and shall hold First Party harmless from any and all damages resulting from the negligence acts of the Second Party or its agents and employees. Upon completion of logging any definite tract Second Party agrees to leave such land, tract or tracts in such condition that certificate of clearance can be obtained from the State departments pertaining to logging and fire.

All logs when cut shall be branded or stamped with a brand or stamp suitable to the First Party, and absolute title and control of all logs, until sold and paid for, shall rest in the First Party.

All Select, Number One (1) and Number Two (2) Sitka Spruce logs are to be delivered to the mill of E. K. Bishop Lumber Company, Aberdeen, Washington. All other Sitka Spruce and all Western Red Cedar logs are to be delivered to any mill

or mills on Willapa Harbor, such mill or mills to be designated by First Party.

Second Party agrees to operate at least Forty Eight (48) hours per week and to do each and everything necessary to log and deliver said logs to the various mills and agrees to construct and maintain all necessary roads, furnish all necessary equipment and supplies, do all falling, bucking, yarding, loading, trucking, booming, rafting, scaling and towing and to pay when due all labor, state and federal taxes of every kind and nature whatsoever, including but not limited to industrial insurance, unemployment compensation, medical aid, and agrees to keep said logs free from any and all claims, liens or liability.

The Parties hereto agree that from the total net cash returns from the sale of all logs shall be deducted stumpage of Seven Dollars Fifty Cents (\$7.50) on all Sitka Spruce logs and Four Dollars (\$4.00) on all Western Red Cedar logs, plus One Dollars (\$1.00) on all logs, per thousand feet board measure, and that after such deductions the balance shall be paid by First Party to Second Party for this service, such payments to be made within ten (10) days after said logs are rafted and scaled, such scaling to be done by any recognized scaling bureau, to be selected by First Party.

Time is of the essence of this contract and Second Party agrees to start operations promptly and continue said logging without interruption, barring such factors as bad weather or strikes which are beyond Second Party's control.

It is expressly understood and agreed that in all its logging operations hereunder the Second Party acts as and is an independent contractor and nothing herein contained shall operate to make the Second Party an agent of the First Party or to be construed as authorizing or empowering the Second Party to obligate or bind the First Party in any manner whatsoever. It is expressly understood and agreed the First Party and Second Party are not partners or principal or agent.

Neuskah was a subsidiary of E. K. Bishop Lumber Company. On January 31, 1946, Neuskah assigned its contract with Rayonier to E. K. Bishop Lumber Company and thereafter McKay and Carlen dealt with the assignee with regard to the contract. The assignment was approved by Rayonier.

On November 1, 1946, August 15, 1948, and October 25, 1948, Rayonier and E. K. Bishop Lumber Company entered into additional contracts similar in material respects to the contract between Neuskah and Rayonier. At the time these additional contracts were entered into E. K. Bishop Lumber Company immediately entered into an agreement with McKay and Carlen for the logging of the areas described in the contracts between Rayonier and Bishop. The agreements with McKay and Carlen were oral and contemplated terms and conditions similar to those stated in the contract of April 23, 1945, between Neuskah and McKay and Carlen. Under the basic contracts between Rayonier and Neuskah and E. K. Bishop, Neuskah and Bishop

retained the spruce for themselves, but resold all the hemlock and cedar to Rayonier at the market price.

McKay and Carlen faithfully performed its contracts and payments have been made in accordance therewith, including the service charge of \$1 per thousand board feet to Neuskah (later E. K. Bishop Lumber Company). McKay and Carlen logged the timber at their own expense and charged all of the costs, including road building, to current operating expenses. They received the net cash returns from the sale of the logs, less the stumpage charge agreed upon and a service fee deducted by E. K. Bishop Lumber Company, which conducted all the selling, collected the proceeds, and remitted to McKay and Carlen the net amount.

McKay and Carlen elected to report their gains on the sale of timber under the various contracts under Section 117 (k).

Opinion.

Tietjens, Judge: The issue for decision is whether the taxpayers may properly treat the cutting of timber under the contracts between the partnership and Neuskah and E. K. Bishop Lumber Company "as a sale or exchange of such timber" as provided in section 117 (k) (1).¹ See also section 117 (j) (1).²

¹ (k) Gain or Loss in the Case of Timber or Coal.—

(1) If the taxpayer so elects upon his return for a taxable year, the cutting of timber (for sale or for use in the taxpayer's trade or business) during

If so, they were entitled to treat their gains as capital gains.

In summary, the taxpayers' argument is that they are entitled to the benefits of 117 (k) (1) "either

such year by the taxpayer who owns, or has a contract right to cut, such timber (providing he has owned such timber or has held such contract right for a period of more than six months prior to the beginning of such year) shall be considered as a sale or exchange of such timber cut during such year. In case such election has been made, gain or loss to the taxpayer shall be recognized in an amount equal to the difference between the adjusted basis for depletion of such timber in the hands of the taxpayer and the fair market value of such timber. Such fair market value shall be the fair market value as of the first day of the taxable year in which such timber is cut, and shall thereafter be considered as the cost of such cut timber to the taxpayer for all purposes for which such cost is a necessary factor. If a taxpayer makes an election under this paragraph such election shall apply with respect to all timber which is owned by the taxpayer or which the taxpayer has a contract right to cut and shall be binding upon the taxpayer for the taxable year for which the election is made and for all subsequent years, unless the Commissioner, on showing of undue hardship, permits the taxpayer to revoke his election; such revocation, however, shall preclude any further elections under this paragraph except with the consent of the Commissioner.

² (j) Gains and Losses From Involuntary Conversion and From the Sale or Exchange of Certain Property Used in the Trade or Business.—

(1) Definition of Property Used in the Trade or Business.—For the purposes of this subsection, the term "property used in the trade or business" * * * includes timber with respect to which subsection (k) (1) or (2) is applicable.

on the basis that [they] purchased the timber and were the owners thereof at all times (subject to the reservation of title for security purposes) or had a contract right to cut such timber and to sell the timber or logs in the normal course of taxpayers' business."

The Commissioner's position is that the contracts involved were essentially to perform services for compensation and that the partnership did not acquire any interest in the standing timber or the logs as cut which would entitle it to capital gains treatment under the subsection in question.

The question is one of first impression and we have no decided cases to serve as guide posts. Cases such as Springfield Plywood Corporation 15 T.C. 697, which was concerned with section 117 (k) (2), where the decisive question was whether there had been a "disposal" of timber by the owner under a contract by which the owner retained an "economic interest" in the timber, are not controlling here. Both parties agree that section 117 (k) (2) has no application to the situation before us.

We look to Regulations 111, section 29.117-8(a), but find little help. The regulations hardly do more than follow the language of the statute.

Some assistance can be found in that part of the report of the Finance Committee of the Senate, Revenue Bill of 1943, 78th Congress, 1st Session, Report No. 627, dealing with section 117 (k) (1). There the following statement appears, at page 25:

Your committee is of the opinion that various timber owners are seriously handicapped under the Federal income and excess profits tax laws. The law discriminates against taxpayers who dispose of timber by cutting it as compared with those who sell timber outright. The income realized from the cutting of timber is now taxed as ordinary income at full income and excess profits tax rates and not at capital gain rates. In short, if the taxpayer cuts his own timber he loses the benefit of the capital gain rate which applies when he sells the same timber outright to another. Similarly, owners who sell their timber on a so-called cutting contract under which the owner retains an economic interest in the property are held to have leased their property and are therefore not accorded under present law capital-gains treatment of any increase in value realized over the depletion basis.

Our attention also has been called to *Boeing vs. United States* (Ct. Cls. 1951), 98 F. Supp. 581, where the Court of Claims in dealing with section 117 (k) (2) and not with our specific problem said: The legislative history of 117 (k) indicates that Congress' principal purpose was to afford relief to timber owners.

These quotations do not decide the question. Nevertheless, they seem to fortify the Commissioner's position that unless the taxpayers can be considered as owners of the timber or as persons having a contract right to cut the timber for sale or for use in their own trade or business they are not entitled to claim the benefits of the section.

We do not think the taxpayers were the owners of the timber. Original ownership was in Rayonier Incorporated. Rayonier, in its contracts with Neuskah and E. K. Bishop Lumber Company, specifically sold the timber to those parties, agreeing at the same time to buy back certain species and appropriate language indicating a sale was employed in those contracts. We do not find language importing a sale in the arrangements between the McKay and Carlen partnership and Neuskah and E. K. Bishop. The taxpayers attempt to explain this discrepancy by pointing out that the original written agreement between the partnership and Neuskah, on which the subsequent oral agreements were based, was drafted by a person unskilled in legal terminology. However that may be, it is stipulated that the partnership's business was "logging timber". That term as explained in oral testimony may or may not encompass cutting timber for sale, but on this record we do not think the partnership had any timber for sale. To be sure, McKay and Carlen had a contract to cut the timber in question, but we cannot find that they owned the timber or had any proprietary interest which would permit them to sell it. All sales were made by Neuskah or E. K. Bishop Lumber Company. McKay and Carlen never had any contact with the purchasers, except insofar as E. K. Bishop invoiced itself for logs it retained. This seems simply to have been for bookkeeping purposes and did not purport to evidence a sale by the partnership to Bishop. Absolute title and control of all logs until sold and paid for

remained under the contracts with Neuskah or Bishop. The taxpayers say this was for security only, but we cannot agree.

The agreement between Neuskah and the partnership is essentially a logging arrangement and the amounts payable to the partnership thereunder are said in the contract to be paid "for this service". We conclude that the essence of the arrangement was that the partnership was employed to cut timber on lands of another for compensation determined on the basis of market price of the logs and that the partnership did not own or have any proprietary interest in the timber, either before or after cutting. The statute speaks of the cutting of timber for sale by a taxpayer who has a right to cut such timber. To us this means that the taxpayer who would claim the benefit of the statute must be the one who has not only the right to cut but also the right to sell on his own account. The taxpayers here were not such persons. We agree with the Commissioner that the statutory language does not cover a taxpayer who cuts timber in which he himself has no proprietary interest which he can dispose of by sale.

Neither, in our opinion, can the petitioners qualify as taxpayers cutting the timber "for use in the taxpayer's trade or business" as required by the statute. They were loggers and were cutting timber which belonged to others and was to be used by others. The taxpayers themselves did not use the timber and they had no control over it except to

cut and deliver it according to the terms of their cutting contracts with Neuskah and E. K. Bishop.

We conclude and hold that the petitioners are not entitled to the benefits of section 117 (k) (1) and approve the action of the Commissioner in this respect.

Reviewed by the Court.

Decision will be entered under Rule 50.

The Tax Court of the United States
Washington

Nos. 37662, HELGA CARLEN; No. 37663, JOHN T. CARLEN; No. 37664, CATHRYN McKAY; No. 37665, ARTHUR R. McKAY; No. 42122, ARTHUR R. and CATHRYN McKAY; No. 42123, JOHN T. and HELGA CARLEN,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the determination of the Court, as set forth in its Opinion promulgated May 29, 1953, the parties having filed on June 23, 1953, an agreed computation of tax, now, therefore, it is

Ordered and Decided: That there are deficiencies

(b) John T. Carlen and Helga Carlen were at all times herein, husband and wife and residents of Raymond, Washington.

2. (a) Arthur R. McKay and Cathryn McKay, as members of a marital community, filed separate income tax returns for the calendar year 1947 with the Collector of Internal Revenue, Tacoma, Washington. For the calendar years 1948, 1949 and 1950 they filed joint returns with the Collector of Internal Revenue, Tacoma, Washington.

(b) John T. Carlen and Helga Carlen, as members of a marital community, filed separate income tax returns for the calendar year 1947, with the Collector of Internal Revenue, Tacoma, Washington. For the calendar years 1948, 1949 and 1950 they filed joint returns with the Collector of Internal Revenue, Tacoma, Washington.

3. The income tax returns of the petitioners and the partnership returns of McKay and Carlen may be admitted in evidence, and identified as follows:

Exhibit A—1947 income tax return of John T. Carlen.

Exhibit B—1947 income tax return of Helga Carlen.

Exhibit C—1948 joint income tax return of John T. and Helga Carlen.

Exhibit D—1949 joint income tax return of John T. and Helga Carlen.

Exhibit E—1950 joint income tax return of John T. and Helga Carlen.

Exhibit F—1947 income tax return of Arthur R. McKay.

Exhibit G—1947 income tax return of Cathryn McKay.

Exhibit H—1948 joint income tax return of Arthur R. and Cathryn McKay.

Exhibit I—1949 joint income tax return of Arthur R. and Cathryn McKay.

Exhibit J—1950 joint income tax return of Arthur R. and Cathryn McKay.

Exhibits K, L, M, and N—Partnership returns of McKay and Carlen for fiscal years ended April 30, 1947, April 30, 1948, April 30, 1949 and April 30, 1950, respectively.

4. Arthur R. McKay and John T. Carlen formed an oral general partnership as of May 1, 1945, to engage in logging in Southwest Washington. Said partners were equal partners. Said partnership had a fiscal year ending April 30. Said partnership continued during all the years here involved.

5. The income taxes in dispute as set forth in the respective notices of deficiency are:

Year	Taxpayer	Amount
1947	Arthur R. McKay.....	\$ 561.52
1947	Cathryn McKay	561.52
1947	John T. Carlen.....	548.01
1947	Helga Carlen	548.00
1948	Arthur R. and Cathryn McKay.....	3,928.78
1948	John T. and Helga Carlen.....	3,904.26
1949	Arthur R. and Cathryn McKay.....	3,071.61
1949	John T. and Helga Carlen.....	3,093.50
1950	Arthur R. and Cathryn McKay.....	1,405.86
1950	John T. and Helga Carlen.....	1,401.90

In the event that the final decision in these cases

is that taxpayers are not entitled to the benefit of Section 117 (k) of the Internal Revenue Code, then the respective tax liability for the taxpayers for the taxable years herein considered is in the exact amount of the tax asserted in the respective notices of deficiency.

6. In the event that the final decision in these cases is that taxpayers are entitled to the benefit of Section 117 (k) of the Internal Revenue Code, then because of certain adjustments it is agreed that recomputation may be submitted under Rule 50 of the Tax Court's Rules of Practice.

7. The single issue in this series of cases is the right of the taxpayers to the benefit of Section 117 (k) of the Internal Revenue Code in computing the income of the partnership, McKay and Carlen, and in computing the tax liability of the partners for each of the years herein involved. It is conceded that the timber in question was valued by the petitioners at the fair market value of said timber as of the first day of each fiscal year, with the exception of the Cedar logged during the fiscal year ended April 30, 1947, which has been conceded by petitioners to have had a market value of \$5.00 per thousand feet, rather than \$10.58 per thousand feet as claimed on the partnership return, on the first day of the fiscal period.

8. Section 117 (k) (1) and (2) of the Internal Revenue Code is the controlling section here involved. The applicable Regulations are Regulations 111, Section 29.117-8.

9. Taxpayers elected in their respective income

tax returns and in the partnership income tax returns for the years involved to report their gain on the sale of timber under Section 117 (k) of the Internal Revenue Code.

10. The partnership of McKay and Carlen was during all years herein involved in the trade or business of logging timber.

11. The partnership of McKay and Carlen was formed to engage in the logging and cutting of timber. On March 15, 1945, Rayonier Incorporated and Neuskah Timber Company entered into a contract, herein attached as Exhibit 1, and made a part hereof, by the terms of which contract Neuskah purchased from Rayonier all of the merchantable cedar and spruce timber and certain hemlock on Sections 29 and 30, Township 13 North, Range 9, W.W.M., Pacific County, Washington, for \$7.50 per thousand board feet for spruce, \$4.00 per thousand for cedar and \$1.50 per thousand for hemlock. Title to the timber was to pass upon cutting. On April 23, 1945, Neuskah Timber Company entered into a contract with McKay and Carlen for the cutting of the timber included in the contract of March 15, 1945, between Rayonier and Neuskah, except for the timber on the south half of Section 29. Said contract between Neuskah and McKay and Carlen is set forth as Exhibit 2, and made a part hereof. Said contract of April 23, 1945, between Neuskah and McKay and Carlen was subsequently orally amended to include the logging of hemlock at \$1.50 per thousand board feet. The timber cut under the contract of April 23, 1945, carried the brand "GH5".

12. McKay and Carlen faithfully performed said contract with Neuskah (later E. K. Bishop Lumber Company) and built and maintained during the term of the contract all roads necessary for the conduct of the logging operations of McKay and Carlen under the terms of said contract without reimbursement. Road building was started in May of 1945 and the first load of logs cut under the Neuskah contract came out on June 5, 1945. For example, under contract GH, the partnership constructed $211\frac{1}{2}$ stations or 21,150 feet of road at the sole expense of the partnership. In addition to road building, the partnership built the necessary spar tree rigging, land preparation, camp site, and colddecks. All the costs of building and maintaining roads necessary for the conduct of logging operations were charged to current operating expense on the partnership books and the partnership income tax returns of McKay and Carlen.

13. McKay and Carlen in addition to making the payments required by the various agreements paid \$1.00 per thousand board feet to Neuskah (later E. K. Bishop Lumber Company) as a service fee, as stated in Exhibit 2. During the fiscal year ended April 30, 1947, this service fee amounted to the sum of \$8,861.25.

14. Neuskah Timber Company, Inc. was a subsidiary of E. K. Bishop Lumber Company and on January 31, 1946, assigned the contract entered into between Rayonier Incorporated and Neuskah on March 15, 1945, to E. K. Bishop Lumber Company and thereafter McKay and Carlen dealt with

E. K. Bishop Lumber Company in place of Neuskah with regard to the contract entered into between Neuskah and the partnership dated April 23, 1945. A copy of the foregoing assignment is attached hereto as Exhibit 3.

15. E. K. Bishop entered into additional contracts with Rayonier for the purchase of timber in Pacific County and copies of these written contracts are included herein as Exhibits as follows:

Exhibit Number	Date	Brand
Exhibit 4	November 1, 1946.....	R9
Exhibit 5	August 15, 1948.....	GH10
Exhibit 6	October 25, 1948.....	GH11

In each case E. K. Bishop Lumber Company immediately entered into an agreement with McKay and Carlen for the logging of the areas included in these additional contracts between Rayonier and E. K. Bishop Lumber Company. The agreement made between E. K. Bishop Lumber Company and McKay and Carlen was an oral agreement in each instance, made at the time that E. K. Bishop Lumber Company entered into its contracts with Rayonier. These oral agreements contemplated terms and conditions similar to those stated in Exhibit 2, except that the subsequent agreements adjusted the rates of payment by McKay and Carlen as follows:

Contract	Species	Price
R9	Spruce	\$ 7.50 and \$3.00 per M
	Cedar	4.00 per M
	Hemlock	2.50 per M
GH10 and GH11	Spruce	12.00 and 4.00 per M
	Cedar	7.00 per M

16. McKay and Carlen elected to report their gains on the sale of timber under the various contracts under Section 117 (k) of the Internal Revenue Code and now concede that if the partnership and the partners are otherwise entitled to the provisions of Section 117 (k), that they are entitled to apply Section 117 (k) only with regard to the timber cut under the following contracts identified by brand for each of the years involved:

FY April 30, 1947.....	GH5
FY April 30, 1948.....	GH5 and R9
FY April 30, 1949.....	GH5 and R9
FY April 30, 1950.....	GH5, R9, GH10 and GH11

17. The timber cut by McKay and Carlen under each contract during each partnership year under the contracts for which the provisions of Section 117 (k) are sought to be applied by taxpayers is set forth in attached exhibits as follows:

Exhibit 7.....	FY April 30, 1947
Exhibit 8.....	FY April 30, 1948
Exhibit 9.....	FY April 30, 1949
Exhibit 10.....	FY April 30, 1950

18. McKay and Carlen performed their various agreements with Neuskah and E. K. Bishop Lumber Company in accordance with the terms of the agreement identified as Exhibit 2. Payments were made in accordance with the terms of the agreement including the service charge and the stated rates for the various timber species. The balance of the market value of the timber was paid to McKay and Carlen.

19. The partnership owned and acquired certain

heavy logging and roadbuilding equipment and the individual partners owned additional heavy logging and roadbuilding equipment which was made available to the partnership. In addition the partnership from time to time rented equipment from third parties.

/s/ CHARLES F. OSBORN,
Counsel for Petitioner.

/s/ CHARLES W. DAVIS,
Chief Counsel,
Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed Oct. 8, 1952.

[Title of Tax Court and Cause.]

TRANSCRIPT OF PROCEEDINGS

United States Court of Appeal Bldg., United States Courthouse, Seattle, Washington, October 8, 1952—11:30 a.m.

(Met pursuant to notice.)

Before: Honorable Norman O. Tietjens, Judge.

Appearances: John H. Welch, Seattle, Washington, appearing for the Respondent. Charles F. Osborn, Seattle, Washington, appearing for the Petitioner. [1*]

The Court: We will be in order.

The Clerk: 37662, Helga Carlen; 37663, John

* Page numbering appearing at the top of page of original Reporter's Transcript of Record.

T. Carlen; 37664, Cathryn McKay; 37665, Arthur R. McKay.

Mr. Osborn: Charles F. Osborn, appearing for the petitioner.

Mr. Welch: John H. Welch, appearing for the respondent.

The Court: Mr. Osborn, did you wish to make an opening statement?

Mr. Osborn: Yes, your Honor.

Opening Statement on Behalf of the Petitioner
By Mr. Osborn

Mr. Osborn: May it please the Court, there is actually cases on the Calendar and these have been consolidated, with two additional cases, which are docket cases and the pleadings have been completed, but are not on the Calendar, because the same issue is involved for all of these taxpayers for all years involved, and is the only issue. That issue is the right of these taxpayers to take——

The Court: The other two cases that are not on this docket, you mean you have stipulated that depending on the result here, those cases will be disposed of?

Mr. Osborn: That is correct, your Honor, and in the docket, in the heading on our stipulation we have added those additional two cases. [2]

All these cases have to do with the application of Sec. 11-7K of the Internal Revenue Code. That is the Timber Section, which permits taxpayers under certain circumstances to report the difference between the cost of their timber and the fair market

value of their timber on the first day of each taxable year and to report that difference as capital gain, long-term capital gain, if held over six months and the question involved here is the right of these taxpayers, who incidentally operated in a partnership, McKay and Carlen, to the benefits of this section. The facts in the case have been substantially stipulated, with numerous exhibits. We intend to put on two witnesses to take care of the several points upon which an agreement was not arrived at.

I would like the Court's indulgence for a brief outline of the history of the logging industry in the State of Washington. It will take just several minutes, your Honor, to give you a little better picture of the operation of the petitioners.

When there were vast stands of timber in the State of Washington the large logging companies could economically log these timbers, log this timber, themselves. They would naturally log the easily accessible areas first. And years ago, what was regarded as merchantable timber was considerably different than what it is today. In other words, they would take out the large-sized logs and they would take out what was regarded as [3] the preferable species, for example, fir. Hemlock, for example, was never taken out except for pulp until World War II, when they learned how to dry hemlock and to cut it into lumber. Unfortunately the vast stands of timber in the State of Washington are disappearing. However, many of the large

logging companies have retained ownership of logged-off lands and those areas which are inaccessible by old-line methods of logging. They never decided to log those areas because the logging costs were too high and as long as there was easily accessible timber, why, they neglected these areas. They have continued to hold these timber lands for a number of reasons. Sometimes they expected real estate development, sometimes they expected to log the second growth. Sometimes they expected to use the land and did use the land for reforestation programs, perpetual logging. In other cases they have held the lands, expecting market conditions to change and someday go back and log this inaccessible timber.

Today in the State of Washington these large logging companies are no longer doing their own logging to a great extent. They are employing small operators, independent operators and the petitioners herein, McKay and Carlen, belong to that classification, sometimes called a gyppo logger, with no reflection whatsoever on my clients. The so-called gyppo logger may log under a situation where he, himself, drives a tractor, he may operate a donkey engine, he may actually do the hand work, [4] with perhaps a crew as small as three or four men, sometimes fifteen men. He generally doesn't set up an expensive operation, he doesn't have a bunkhouse, he doesn't have a cookhouse. He often employs local people in the area. And these larger companies today want to get all the merchantable timber off their remaining lands and to do so they

will employ the so-called gyppo logger to remove that timber.

Now, there are various types of contracts that these major logging companies and the gyppos enter into. Sometimes it is what is called a service contract. The large timber owner will build the roads into the timber and he may contract with a gyppo to remove the desired timber at so much a thousand, maybe thirty or forty dollars a thousand. That assures the gyppo recovering his costs and perhaps making a profit. It likewise protects the timber owner in that he can control the operation by supervision and keep control of the logs.

Another type of gyppo contract is one in which the gyppo purchases the timber and the underlying real estate and agrees to remove the logs and to sell the logs back to the original owner.

A third type is one in which the large timber owner sells only the timber and retains title to the real estate and obligates the gyppo contractor or logger to remove the logs and generally to sell back the logs or a certain species of the logs back to the original owner of the land. [5]

Sometimes there is a variation of these three principal types of contracts. In any event, the mills want these logs removed and they are not in a position to do it themselves, because these areas are the remaining inaccessible areas. They are very small operations which do not justify large crews.

In this particular case the so-called large timber owner, is Rayonier, Incorporated, one of the large

timber owners in the State of Washington, also engaged in pulp manufacture.

Because of the shortage of timber there is often arrangements made between the leading companies to exchange timber. Sometimes a company like Rayonier which wants hemlock logs for pulp may make an arrangement with another large operator to purchase hemlock and in return to sell to the second operator a species of log that the second operator wants and in this case we have that situation. A second large timber owner called Bishop Lumber Company, the evidence will show, was primarily interested in spruce logs, because it had a spruce mill operation. McKay and Carlen have no logs, no timber, at the time that the basic contracts we are going to consider were entered into. They were simply experienced loggers. So the facts will show that Rayonier entered into a contract with Bishop for the sale by Rayonier to Bishop of certain logs on certain tracts of land. The facts will further show that Bishop did not do any of the logging itself, that it entered into an agreement with the petitioners herein, McKay and Carlen, to do the actual logging. Now, when I mention the company Bishop, just to clarify your thinking, your Honor, there is an earlier contract with a company called Neuskah, which takes the place of Bishop. The original contract was between Rayonier and Neuskah, and Neuskah is a subsidiary of Bishop Lumber Company, and after the first year Neuskah disappears from our consideration and all further contracts between Rayonier and the next operator were between Ray-

onier and Bishop. There are four contracts here to consider. But in all four contracts, the first one with Neuskah and the second, third and fourth ones with Bishop, McKay and Carlen took over and conducted the actual logging operation.

Now, the principal point to be considered is whether this contract that McKay and Carlen had first with Neuskah and later with Bishop, entitled them to the benefits of Sec. 11, 7-K. It is our contention that under the contract with Neuskah and later the contracts with Bishop, that McKay and Carlen not only agreed to remove the timber but that they actually purchased the timber and that when the timber was dead and down, they sold that timber or sold the logs back to, partly to Bishop, partly to Rayonier and partly to third parties, and that they paid what is called a stumpage price for the timber, that is, they paid to Rayonier, who was the owner of the standing timber so much per thousand for each species of timber removed and the stipulation sets out those arguments. They also paid a service charge to Bishop to handle their paper work in connection with this arrangement. And there were certain other charges, fluming and rafting charges and the net proceeds after the payment of the stumpage and these other charges was the property of McKay and Carlen and they stood to lose or to make money, depending upon the market price that they received for the logs. There was no agreement in any of the contracts fixing the market price. The market price was to be the prevailing market price at the time.

Substantially, your Honor, that is a basic outline of the facts and issues herein presented.

The Court: Thank you.

Mr. Welch, do you have anything to add?

Mr. Welch: A brief statement, your Honor.

Opening Statement on Behalf of the Respondent
by Mr. Welch

Mr. Welch: As Mr. Osborn stated, the majority of the facts in this case have been stipulated.

The Court: Do you agree with him on the summary of the history of logging in Washington?

Mr. Welch: I am not as well acquainted as he is, but I have made some inquiry and I think he has made a fair statement as to the background of the industry.

Now, getting right to the point of the case, the Statutory Notice, of course, which states our position in all of these dockets, that brings out the point that the Government's position is that the, that Carlen and McKay had no economic interests in this timber and to develop that a little farther, it is our contention that this contract, the series of contracts which Carlen and McKay had with the E. K. Bishop Lumber Company and with Neuskah in the earlier period were contracts to perform services. And we will argue the case on that basis, that the ownership of the timber was always with Rayonier or Bishop and that the services performed by Carlen and McKay do not invest any form of legal ownership in the timber in them and for that reason it would be impossible to apply the provisions of Sec. 11, 7-K in such a manner that they would be able to claim the capital gains, under the circumstances.

I think that is all I have.

The Court: You may call your witnesses.

Mr. Osborn: Mr. McKay.

The Court: Do you want to offer the stipulation now?

Mr. Welch: We have entered into a stipulation which contains agreement on most of the facts. I have two copies I would like to hand to the Court at this time.

The stipulation in one of the paragraphs states that the tax returns of Carlen and McKay as a partnership and the returns of the individuals for the four years there in controversy may be admitted without further identification and they are each assigned a letter number in the stipulation. **Would** you prefer that I call these off or that, those would be Respondent's Exhibits A through N, or should I just hand them to the Clerk and have them be marked?

The Court: Are they made part of the stipulation?

Mr. Welch: They are designated in the stipulation by the same letter that's shown on the return.

The Court: I don't think it would be necessary, then, for the Clerk to remark them.

Do you offer them along with the stipulation?

Mr. Welch: I offer them along with the stipulation, yes.

The Court: I understood Mr. Osborn to say that these cases had been consolidated.

Mr. Osborn: By stipulation, your Honor.

Mr. Welch: The stipulation itself does not specifically state in there, except that all of the docket

numbers are shown in the heading of the stipulation. That would include two additional docket numbers for Mr. Carlen and Mr. McKay, for three subsequent years. They're all consolidated in the Statutory Notice, so actually instead of having one year before the Court we have four years before the Court on the same or similar issue.

The Court: Then I will take it, it is agreed that these cases will be heard together and considered to go and decided together.

Mr. Osborn: Yes, sir, your Honor.

Mr. Welch: Yes, sir. [10]

The Clerk: You mean with these two additional cases that are included in here? They have included two cases that are not on this docket, on this Calendar.

The Court: That is the only thing that bothers me, is how to handle those two additional cases which have not been docketed on this Calendar.

Mr. Osborn: The pleadings are completed, your Honor, and we have gone into some length in the stipulation to set out the deficiencies involved. The factual presentation is identical with all of the years involved.

The Court: We will take what steps are necessary to have those cases assigned to this Calendar so we can consider them.

Will you take that up with the Clerk's Office in Washington, Mrs. Silberg.

Mr. Osburn: Mr. McKay, would you please come forward? Whereupon,

ARTHUR R. MCKAY

called as a witness for and on behalf of the petitioners, having been first duly sworn, was examined and testified as follows:

Q. By Mr. Osborn: Mr. McKay, where do you reside?

A. Aberdeen, Washington.

Q. Generally in what area of the State of Washington is that located? [11]

A. In the southwest part.

Q. Do you still have some timber down there?

A. Yes.

Q. Not very much, I suppose?

A. No, it is getting a little scarce now.

Q. Mr. McKay, as of May 1, 1945, what was your business?

A. Well, around May 1 of '45, John Carlen and I formed a partnership to remove and purchase and sell timber from a contract with the Neuskah Timber Company.

Q. Have you been a partner at all times since May 1, 1945, with Mr. Carlen?

A. Yes, I have.

Q. What was the purpose of forming the partnership on May 1 of '45?

A. Well, prior to May 1, 1945, we had, we each had equipment which we rented out at so much an hour and operated ourselves.

Q. What kind of equipment?

A. That was Caterpillar tractors and we both built roads and logged. About that time we were

(Testimony of Arthur R. McKay.)

running out of work for this particular company we were working with, so we started looking for timber to log ourselves. And through the cooperation of the Bishop Lumber Company we obtained this tract of timber out of Raymond, Washington.

Q. And since May 1 of 1945, through April 30, 1950, did you carry on a logging operation in this general area of Raymond, Washington? [12]

A. Yes, we did.

Q. Mr. McKay, I hand you a copy of Petitioners' Exhibit 2, which is a part of the stipulation, which is a contract between the Neuskah Timber Company and McKay and Carlen. Would you tell the Court in your own words, what were the circumstances surrounding the execution of that contract?

A. Well, as I told you before, we had been logging around for a contract, or for timber to buy and we located this timber in Raymond that was somewheres near where we had worked before, and due to the fact that, that we were gyppo loggers, as they call us, it was impossible for us to go out and purchase timber, and the only way we could get it was through some other mill which had ways and means of swinging deals. And it so happened that we had worked for the Bishop Company before and due to the fact they had trading stock or hemlock timber that they could trade for spruce timber that was on this particular section that we were looking at, they helped us make the deal.

Q. Who prepared that particular contract, Mr. McKay?

(Testimony of Arthur R. McKay.)

A. The accountant, Mr. Maw. And that contract was——

Q. I was asking you, who prepared the contract, Mr. Maw and yourself?

A. Mr. Maw and myself, yes.

Q. Did you have the benefit of counsel at that time? [13]

A. No, we didn't.

Q. What was your understanding as to your obligation assumed under the terms of that contract?

A. Well, we were to remove and purchase and sell the timber and we were to build our own roads and open up the country ourselves, all at our expense.

Q. Did you understand that you were to remove all of the merchantable timber on the described tract of land?

A. Yes, we were to remove all merchantable timber on the north half of Section 29 and Section 30, which was in the original contract.

Q. Did this type of contract differ from other so-called gyppo contracts with which you had had previous experience, and if so in what way?

A. This contract was entirely different than any contract we had had before. Those that we had had previous, there was a stipulated amount that we were to receive for our services and the companies that we worked for put the access roads in to the timber. But on this deal we had to lay out our own roads, we had to build our own roads, we had to hire trucks, and we had to hire shovels to ballast the

(Testimony of Arthur R. McKay.)

road, and due to the fact that we were buying it on stumpage prices, there was a stipulated price on the price of the stumpage, and that we were, you might say, gambling on what the net results would be, due to the fact that we didn't know what the market price would be. [14]

Q. And you expected to make a profit from this type of contract?

A. Well, using the experience that he had had in the past in logging and using the equipment, we had it pretty well doped out as to what our costs would be and we were sure that the price of the stumpage was fair. And with the present selling price of logs, at that time, we were quite sure that we could make it, and it looked like that the price of logs was going up, which it did.

Q. What brought about the anticipated rise in the price for logs?

A. Well, when the O.P.A. went off, of course, there wasn't any regulations on the price of logs at that time and the demand was so great that the mills started to bid higher on them.

Q. Was there a shortage of fallers and buckers and logging crews during the years involved herein?

A. Well, especially in the first two years, it was terrible, it was hard to get men and those that you did get weren't too reliable.

Q. Were you in a position to negotiate more favorably with Neuskah and Bishop in the years involved here than you otherwise would have been because of these other circumstances?

A. Well, I think so, because they had been in the

(Testimony of Arthur R. McKay.)

logging business themselves and they had a lot of trouble in getting men to work for them, and their primary interest was in the [15] spruce logs to use in their mill. They weren't interested in the logging part of it. So through those connections, why, we were able to make that kind of a deal.

Q. If the market and the log prices had dropped and you had suffered a loss, who would have borne that loss?

A. Well, we would have.

Q. Who built the roads in connection with your logging operation?

A. We built them all. We laid the roads out, spent considerable time laying the country out and finding where the roads should be located, and then we hired men to go in and fall right-of-ways, below the stumps, furnished our own Cats for building the grade, but we did have to hire the trucks and shovels to ballast the roads.

Q. Were you reimbursed for the construction of these roads? A. No.

Q. How far in advance did you normally build these roads?

A. Well, we generally like to have it at least six months and better yet to have a year ahead, because you can't depend on the weather and the cost of road building is so much cheaper during the summer months.

Q. How much did you actually build ahead?

A. We had six or seven months ahead all the time.

(Testimony of Arthur R. McKay.)

Q. I notice in the stipulation that the term "station" is used. What is the reference to that term?

A. That is an engineering term of a hundred feet.

Q. And I notice in the stipulation that in the first year of the contract you built about 211½ stations. That would be approximately four miles?

A. Yes, 21,000 feet or four miles.

Q. I hand you Exhibit No. 4, which is a part of the stipulation, which is a contract between Rayonier, Incorporated, and E. K. Bishop Lumber Company, executed November 1, 1946. How did McKay and Carlen have an interest in that contract?

A. This contract was turned over to us and——

Q. Turned over to you by whom?

A. By the Bishop Company, and we were to go in there and remove and sell the logs and in turn they were to bill the billings out on them. They billed the logs out to the various companies for us, but the contract was turned over to us.

Q. Did you immediately begin to perform your duties under that contract, shortly after it was entered into?

A. Yes, every time that we got a contract, we have got a contract, we have always went in and started building the roads and locating them in order to have work ahead for the yarding crews.

Q. Was your contract between Bishop and McKay and Carlen in writing or was it oral?

A. The original contract was in writing, but the

(Testimony of Arthur R. McKay.)

various contracts that we had afterwards were oral. [17]

Q. To what contract did you look for the terms and conditions under which you were to log the subsequent contracts?

A. That was entirely given us in oral, we, of course, had the maps of the territory, knew all the country there, and as these various contracts were made out by Rayonier, they were handed to us, and we knew which timber we were to go to next.

A. Did the first original contract of McKay and Carlen and Neuskah Timber Company apply in any respect to these subsequent contracts, these oral contracts?

A. Yes, everything helped, in fact, every condition was the same with the exception of one thing, that on some of the later contracts the price of the stumpage raised in accordance with the market price of the logs.

Q. You mentioned that a service fee was paid to E. K. Bishop Lumber Company and the stipulation points out that that fee was \$1 per thousand. What was the function, excuse me, what was the service that Bishop Lumber Company was to perform in return for this fee of \$1 per thousand?

A. Well, at that time, when we started this particular logging, there was only the two of us. We had two pieces of equipment. We didn't have a regular employed bookkeeper, and it was agreed with them that they should do the billing, take care of the rafting and scaling and in turn charge us, or we would

(Testimony of Arthur R. McKay.)

pay them \$1 a thousand, which we thought was as cheap or cheaper than we could do it because of the inexperience, our inexperience [18] with billing out this particular timber.

Q. Your inexperience?

A. Our particular inexperience.

Q. To save the Court's time, I am going to show you Exhibit 5, which is a contract and—Bishop Lumber Company, dated August 15, 1948, and a contract, Exhibit 6, dated October 25, 1948, between Rayonier and Bishop. And ask that, is your testimony with regard to the relationship of McKay and Carlen to these two contracts substantially the same as your testimony with regard to the relationship of McKay and Carlen in the matter of the contract of November 1, 1946 between Rayonier and Bishop?

A. Our agreements on all these contracts were exactly the same, as I said before, with the exception of on the later ones the price of the various timber raised and that was due to the fact that stumpage was priced out very low from the beginning and as the market prices went up, why, of course, the price of stumpage went up in accordance.

Q. Was it the understanding that you were to remove all the merchantable timber from these various tracts?

A. Yes, we were.

Q. One further question, Mr. McKay, was this \$1 service charge paid to Bishop for handling your sales and invoicing the same regardless of the type or specie of log sold?

(Testimony of Arthur R. McKay.)

A. Yes, it was the same on all of them.

Mr. Osborn: That is all. [19]

Cross-Examination

Q. By Mr. Welch: Mr. McKay, what were your instructions from Neuskah and the Bishop Company, and Rayonier, with relation to where these roads would be laid out?

A. The roads, in the first two or three years, they were all laid out by ourselves. We had no engineers employed, we had the experience ourself, we laid them out to our best advantage, by ourselves.

The Court: You located them yourself?

The Witness: That is right.

Q. (By Mr. Welch) Did you obtain any advice from Mr. Maw at Bishop or from the Rayonier Company?

A. As to where these should be located?

Q. Yes. A. No, sir.

Q. Were all the logs that were cut on this land delivered to Rayonier or E. K. Bishop by you and your partner?

A. No. Of course, Rayonier was primarily interested in hemlock, that is all they used in their operation. Bishop was interested in spruce. That is all he cut. About the only other species there was cedar and it was bought by the various shingle mills or cedar mills.

(Testimony of Arthur R. McKay.)

Q. However, did you not actually make the sales to these other mills? [20]

A. We paid Bishop this dollar a thousand to take care of that for us.

Q. So that you had actually no contact with the various mills that were going to consume the timber?

A. No, we didn't have to do that because we had him employed at a dollar a thousand to take care of it.

Q. And you actually had no control over who the purchaser was going to be, if Rayonier made the decision as to who was to buy the timber, either Rayonier or Bishop?

A. Well, that was primarily understood when we started out. Rayonier we knew would take the hemlock, because we knew that is what they wanted and then Bishop would take the spruce and then there was the cedar, that was the only other that had to be sold to the outside.

Q. Were there any other loggers on this timberland?

A. In the first couple of years there weren't, but later there was one other logger.

Q. He was put on there by Rayonier or by——

A. By Bishop.

Q. Then you didn't do all of the E. K. Bishop Company's logging?

A. No entirely, no.

Q. All the logs were branded in accordance with

(Testimony of Arthur R. McKay.)

the agreement set up between Rayonier and Bishop—

A. That is right, the different locations or different [21] parts of sections had a different brand. Or in other words, too, there was a difference in brand when it come to a change in price, and stumpage, there was a way of cutting off from one price to the other, the various brands.

Q. The brand didn't refer to the particular area from which the log was taken, it referred to the— or did it?

A. I would say it was both. It would pertain to a certain area, because that certain area you were paying so much a thousand for.

Q. I notice you used a brand "R-9" in one instance and also a brand "GH-10" or "GH-11".

A. That would refer to various locations.

Q. Would GH refer to Grace Harbor or—

A. Not necessarily.

Q. And the R had no reference to Rayonier?

A. No. That I couldn't answer you. I wouldn't know.

Q. But those brand names were established between the Bishop and Rayonier Companies?

A. That is right.

Q. With reference to the contract which has been designated Petitioner's Exhibit 4 which is an agreement between Rayonier and Bishop Lumber Company, I would like to direct your attention to the paragraph which is numbered 2, about halfway down the page. Now, is the statement there consist-

(Testimony of Arthur R. McKay.)

ent with your statement that you made on direct examination that you actually [22] purchased this timber from the Bishop Company or from the Rayonier, Incorporated?

A. Now, there is something that I think, I can explain that, too. Here we are a couple of gyppos out there, probably a lot of liabilities and no capital. They had only one way of protecting themselves and the only way they could do it was to hold the title.

Q. In other words, title was actually reserved in Bishop or in Rayonier at all times during these transactions?

A. I would say that. They didn't have any other way of protecting themselves. They couldn't give us a bill of sale for it.

Q. That would interfere with their operations in the sense that perhaps your creditors might attach or place liens on the logs, is that correct?

A. That is true.

Q. Is that your understanding?

A. That is true, yes.

Q. The service fee that was worked out in the contract between you and Neuskah and later E. K. Bishop, that was never actually paid by you and your partner to Bishop, but was deducted from the proceeds of the sale of the logs, is that correct?

A. Yes, that is right, they would, during their billings, rather than then bill us and send them a check, it was deducted [23] at the time they sent us our invoices.

(Witness excused.)

Whereupon,

ROBERT L. AIKEN

called as a witness for and on behalf of the Petitioners, having been first duly sworn, was examined and testified as follows:

Direct Examination

Q. (By Mr. Osborn): Will you state your profession?

A. I am a Certified Public Accountant.

Q. How long have you been engaged in public accounting?

A. Nine years.

Q. And where are you presently located?

A. Aberdeen, Washington.

Q. Where were you located prior to going to Aberdeen? A. Seattle.

Q. And with what firm were you associated?

A. In Seattle?

Q. Yes. A. Haskins & Sells.

Q. When did you go to Aberdeen?

A. December 1, 1945.

Q. In your public accounting experience, are you familiar with logging accounting?

A. I am, sir. [24]

Q. What service did you perform for McKay and Carlen?

A. From December of '45 until about September of '48, I or people directly under my supervision kept all the records for McKay and Carlen. In other words, our firm was the bookkeepers for McKay and Carlen. After, subsequent to that date, my only

(Testimony of Robert L. Aiken.)

working connection with McKay and Carlen was assisting in the preparation of their Federal Income Tax returns.

Mr. Osborn: Would you mark those, please?

(The document above referred to was marked
Petitioners' Exhibit 11 for identification.)

The Clerk: Petitioners' Exhibit 11.

Q. (By Mr. Osborn) I hand you Petitioners' Exhibit 11, marked for identification, and ask you to tell us what that document is.

A. That is an invoice for logs sold to E. K. Bishop Lumber Company, spruce logs.

Q. What relation does that document bear to the operations of McKay and Carlen?

A. Attached to this is a computation, a breakdown, of this invoice. This invoice is, in other words, a complete raft. Attached is a breakdown of the logs belonging to McKay and Carlen, which is included in that particular raft.

Q. How is that indicated, how is it indicated that certain logs belong to McKay and Carlen?

A. By the brand number. All the logs in this particular [25] raft, GH-5, belong to McKay and Carlen.

Q. You received a copy of that invoice in your office, did you?

A. That is right.

Q. What did you do with that invoice?

A. Well, that became a copy of our sales invoice and was entered in our sales journal in the regular course of business.

(Testimony of Robert L. Aiken.)

Q. You stated that you or someone in your employ kept the books for McKay and Carlen during 1945 and subsequent periods. When did you stop that?

A. When did we stop?

Q. Yes.

A. Well, we, I can't give you the exact date. It was, I believe, September of '48. We had an office in Raymond, Washington, and at that time we sold that office, and the files and so forth of McKay and Carlen went along with that sale, so——

Q. Now, with reference to the document which has been marked for identification as Petitioners' Exhibit 11, you stated that that constituted a sale or an invoice resulting from a sale by McKay and Carlen. Now, could you explain just your reasoning on the use of the word "sale" here, on the strength of the document?

A. Well, now, this is a sale, I would assume to the E. K. Bishop Lumber Company. It says "Sold to E. K. Bishop Lumber Company." [26]

Q. Yes, but it is on their letterhead.

A. Well, it is my understanding that McKay and Carlen were paying Bishop to take care of their billing.

Q. You made further reference to the brand numbers on here; you referred to "GH-5." You don't of your own knowledge know whether McKay and Carlen, were the actual owners of the brand number "GH-5," do you?

A. Well, as far as I ever knew, they were the owners of logs branded GH-5, yes.

(Testimony of Robert L. Aiken.)

Q. But your knowledge isn't based on an examination of contracts or agreements or anything of that sort?

A. Well, it is based on examination of the contracts and discussion with McKay and Carlen and various other people that had anything to do with these logs.

Q. But so far as this exhibit is concerned, it does represent a billing from E. K. Bishop Company to E. K. Bishop Company?

A. On the face of it, that is what it says, yes.

Q. And that would be consistent with other testimony that there was never a title of this lumber with McKay and Carlen?

A. I am not qualified to answer that. I don't know. As I said before, as far as I know, the reason it was, the reason it came this way was that McKay and Carlen were paying for that service. We could have done that billing and billed Bishop for it, but it was already taken care of. This became the same as [27] the Accounting Department's copy of the sales invoice right here.

Q. This invoice does detail the service charge that you refer to, is that correct?

A. That is right, this dollar a thousand here, these reference numbers here, "SJ," that has been entered on Sales Journal 27, and the stumpage has been entered on the purchase journal and also other expenses in connection with that.

Mr. Welch: That is all.

Mr. Osborn: I offer in evidence.

(Testimony of Robert L. Aiken.)

The Court: Do you have any objection, Mr. Welch?

Mr. Welch: Yes, I would like to object to this, the admission of this exhibit. My objection is qualified to this extent, that I object to the, any of the, testimony which relates to the use of the words purchase and sale, in connection with the relation between Carlen and McKay and the E. K. Bishop Lumber Company, so the objection is more to the use of the terms than the document itself.

The Court: Well, I will admit the exhibit.

The Clerk: Petitioners' Exhibit 11 admitted.

(The document above referred to as Petitioners' Exhibit No. 11 was received in evidence.)

Mr. Osborn: I would like these marked.

(The documents above referred to were marked Petitioners' Exhibit Nos. 12 and 13 for identification.)

Q. (By Mr. Osborn): I hand you Petitioners' Exhibit 12, [28] marked for identification, which is just to shorten your testimony, if it please the Court, and I also intend to hand you Petitioners' Exhibit No. 13, marked for identification, which appear to be similar in all respects to Petitioners' Exhibit 11, except that the purchasers, or let us say, the invoices indicate the words "sold to Rayonier, Inc." on Petitioners' Exhibit No. 13, and Petitioners' Exhibit No. 12 says "sold to E. C. Miller Cedar Lumber Company." Now, is your testimony with re-

(Testimony of Robert L. Aiken.)

gard to these two invoices substantially the same as your testimony with regard to Petitioners' Exhibit 11?

A. Yes. These are just different companies that have got different species of timber is all, it is the same type of dealings.

Q. (By Mr. Welch): A question, Mr. Aiken, similar to the other question. These exhibits are invoices of a sale between E. K. Bishop Lumber Company and the concern which has been designated after the printed word, "sold to" on the invoice, is that correct?

A. I would say so, yes.

Q. And the only reference to Carlen and McKay on these offered exhibits is the typed matter with reference to the various brand names?

A. This appeared on the copy we got. It didn't of course appear on the copy that Rayonier got (indicating).

Mr. Osborn: I offer these invoices at this time, [29] Petitioners' Exhibit 12 and Petitioners' Exhibit 13 for admission.

Mr. Welch: No objection.

The Court: Admitted.

(The documents above referred to as Petitioners' Exhibits Nos. 12 and 13 were received in evidence.)

Q. (By Mr. Osborn): Just to clarify one point, with reference to those last exhibits, the computation with reference to McKay and Carlen, I pre-

(Testimony of Robert L. Aiken.)

sume, appears only on the copies of the invoices sent to your office or to McKay and Carlen?

A. I would imagine so, yes.

Mr. Osborn: No further questions.

Mr. Welsh: No further questions.

Mr. Osborn: Your Honor, that concludes the petitioners' case.

The Court: Mr. Welch?

Mr. Welch: That concludes the respondent's case.

Mr. Osborn: May I ask the Court's indulgence for 60 day for briefs, inasmuch as I think I will be away for two weeks in November and we will have a delay in obtaining the transcript and the question of communications between here and Washington, D.C.

The Court: Mr. Welch, I take it you are going to be busy, too? [30]

Mr. Welch: It is speculative, I think I will. I would prefer in this case that simultaneous briefs be submitted.

Mr. Osborn: That is satisfactory.

Mr. Welch: And that 60 days would be highly satisfactory to me.

The Court: Well, simultaneous briefs are all right with me so long as the parties don't have a conflict on the suggested findings of fact. In this case where most of the facts are stipulated, I don't see that is going to develop, and I will accept simultaneous briefs in 60 days.

Mr. Osborn: There will be an argument on the ultimate fact.

The Court: 60 days and 30 days to reply.

The Clerk: December 8th and January 7th for reply briefs.

The Court: We will recess until 2 o'clock.

The Clerk: Will you show that photostats may be substituted for Petitioners' 11, 12 and 13.

(Thereupon, at 12:35 o'clock, p. m., the hearing in the above-entitled matter was closed.)

[Endorsed]: T.C.U.S. Filed October 22, 1952.

In The United States Court of Appeals
For The Ninth Circuit

[Title of Causes.]

PETITION FOR REVIEW

John T. and Helga Carlen, and Arthur R. and Cathryn McKay, the Petitioners in the causes above listed, by their counsel, Charles F. Osborn, hereby file their consolidated petition for a review by the United States Court of Appeals for the Ninth Circuit of the decision by the Tax Court of the United States, entered on June 25, 1953, subsequent to an opinion of said Court rendered on May 29, 1953, 20 T. C. No. 77, determining deficiencies in Petitioners' federal income taxes, as follows:

Year	Taxpayer	Docket No.	Amount
1947	Arthur R. McKay	37665	\$ 561.52
1947	Cathryn McKay	37664	561.52
1947	John T. Carlen	37663	548.01
1947	Helga Carlen	37662	548.00
1948	Arthur R. and Cathryn McKay	42122	3,928.78

Year	Taxpayer	Docket No.	Amount
1948	John T. and Helga Carlen	42123	3,904.26
1949	Arthur R. and Cathryn McKay	42122	3,052.04
1949	John T. and Helga Carlen	42123	3,093.50
1950	Arthur R. and Cathryn McKay	42122	1,405.86
1950	John T. and Helga Carlen	42123	1,401.90

The six docketed causes herein were by stipulation heard and decided together, there being but one underlying issue, the same for all taxable years and all taxpayers.

The Petitioners respectfully show:

I.—Venue

Petitioners, Arthur R. McKay and Cathryn McKay are members of a marital community and reside at Aberdeen, Washington. Petitioners, John T. Carlen and Helga Carlen are members of a marital community and reside at Raymond, Washington.

For the calendar year 1947 the members of each community filed separate federal income tax returns. For the calendar years 1948, 1949 and 1950 each community filed joint returns. All returns were filed with the Collector of Internal Revenue, Tacoma, Washington.

II.—Nature of the Controversy

The controversy relates to the proper determination of Petitioners' liability for federal income taxes for the calendar years 1947, 1948, 1949 and 1950.

In 1945, Petitioners, Arthur R. McKay and John T. Carlen, formed a partnership to purchase, log

and cut timber in southwestern Washington. On April 23, 1945 this partnership entered into a contract with Neuskah Timber Company to purchase, log and cut certain standing timber previously purchased by Neuskah, located on the land of a third party.

McKay and Carlen were to remove the timber, build and pay for all necessary roads themselves, and to sell certain designated species to Neuskah (later Bishop) or to Rayonier, Incorporated and had the right to sell species other than those certain designated species, to third parties. McKay and Carlen paid fixed stumpage for the timber as cut and engaged Neuskah (later Bishop) to act as sales agent for the partnership and to handle all invoicing at a fixed rate per thousand.

In January 1946 Neuskah's parent corporation, E. K. Bishop Lumber Company, assumed Neuskah's position vis-a-vis the landowner on the one hand and McKay and Carlen on the other. Thereafter, in 1946 and 1948, McKay and Carlen took additional contracts with Bishop, on terms like the original Neuskah contract.

From 1945 through 1950 the partnership of McKay and Carlen performed the aforesaid contracts. The gain realized under the contracts was reported by Petitioners and their wives, in either separate or joint returns as indicated above, as long term capital gains under Section 117 (k) (1) of the Internal Revenue Code. It is conceded in the Stipulation that Petitioners are not entitled to the provision of Section 117 (k) (1) except as to those contracts held

for more than six (6) months prior to the commencement of each taxable year herein under review.

The Commissioner of Internal Revenue ruled that Petitioners were not entitled to the benefits of Section 117 (k) (1), and that all of the net proceeds of the contracts were ordinary income to Petitioners, and determined deficiencies for the years 1947, 1948, 1949 and 1950, as detailed above.

The Tax Court approved the action of the Commissioner in its opinion promulgated May 29, 1953, and decision was thereupon entered under Rule 50 of the Tax Court Rules of Practice, against Petitioners in all cases, the date of this decision being June 25, 1953.

III.—Assignment of Errors

The Petitioners assign as error the following acts and omissions of the Tax Court of the United States:

1. The finding that Petitioners are not entitled to compute their gain realized on the sale of timber, purchased and cut in accordance with the subject contracts, under Section 117 (k) (1) of the Internal Revenue Code.

2. The finding that Petitioners, through their partnership, McKay and Carlen, were not engaged in the business of cutting timber for sale on their own account.

3. The finding that the cedar logs were to be sold to Bishop.

4. The finding that the partnership of McKay and Carlen did not have any timber for sale.

5. The finding that Neuskah (later Bishop) did not retain title to the timber until cut and sold for security purposes.

6. The finding that the partnership of McKay and Carlen was employed to cut the timber for compensation.

7. The finding of deficiencies against all Petitioners for the years 1947, 1948, 1949 and 1950, in lieu of a determination that there is no income tax due from Petitioners for any of the years in controversy, except as admitted by Petitioners in the Stipulation of Facts.

8. The making and entering by the Tax Court of the United States of its decision is contrary to the evidence and the law.

IV.—Prayer

The Petitioners herein, being aggrieved by the above decision of the Tax Court of the United States, desire to obtain a review of this decision, and of all the proceedings heretobefore had before the Tax Court of the United States, by the United States Court of Appeals for the Ninth Circuit, to the end that the errors and omissions of the Tax Court of the United States may be corrected and that the Tax Court of the United States may be directed to enter an order in each of the above entitled causes showing "No deficiency," except to the extent admitted by Petitioners in the Stipulation of Facts.

/s/ CHARLES F. OSBORN

Counsel for Petitioners

State of Washington,
County of King—ss.

Charles F. Osborn, being first duly sworn, says:

That he is counsel of record in the above named causes; that as such counsel he is authorized to verify the foregoing petition for review; that he has read the petition and is familiar with the statements contained therein; and that the statements made are true to the best of his knowledge, information and belief.

/s/ CHARLES F. OSBORN

Subscribed and sworn to before me this 15th day of September, 1953.

[Seal] /s/ C. CALVERT KNUDSEN

Notary Public in and for the State of Washington,
residing at Seattle.

Service of copy of Petition for Review acknowledged this 17th day of September, 1953.

/s/ KENNETH W. GEMMILL

Acting Chief Counsel, Internal Revenue Service Attorney for Respondent

[Endorsed]: T.C.U.S. Filed September 17, 1953.

The Tax Court of the United States
Washington

[Title of Causes.]

CERTIFICATE

I. Victor S. Mersch, Clerk of The Tax Court of the United States do hereby certify that the foregoing documents, 1 to 30, inclusive, constitute and are all of the original papers and proceedings on file in my office as called for by the "Designation of Contents of Record on Review" in the proceedings before The Tax Court of the United States entitled "Helga Carlen, John T. Carlen, Cathryn McKay, Arthur R. McKay, Arthur R. and Cathryn McKay and John T. and Helga Carlen, Petitioners, vs. Commissioner of Internal Revenue, Respondent, Docket Nos. 37662, 37663, 37664, 37665, 42122 and 42123" and in which the petitioners in The Tax Court proceedings have initiated a consolidated appeal as above numbered and entitled, together with a true copy of the docket entries in said Tax Court proceedings, as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 14th day of October, 1953.

[Seal]

/s/ VICTOR S. MERSCH.

Clerk, The Tax Court of the
United States

[Endorsed]: No. 14090. United States Court of Appeals for the Ninth Circuit. Helga Carlen, John T. Carlen, Cathryn McKay, Arthur R. McKay, Arthur R. and Cathryn McKay and John T. and Helga Carlen, Petitioners, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Petition to Review a Decision of The Tax Court of the United States.

Filed: October 22, 1953.

/s/ PAUL P. O'BRIEN.

Clerk of the United States Court of Appeals for the Ninth Circuit.

In the United States Court of Appeals
for the Ninth Circuit

No. 14090

HELGA CARLEN, et al., Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

STATEMENT OF POINTS

The points upon which appellants intend to rely on appeal are as follows:

1. The Tax Court of the United States erred in finding that appellants are not entitled to compute their gain realized on the sale of timber, purchased and cut in accordance with the subject contracts, under Section 117 (k) (1) of the Internal Revenue Code.

2. The Tax Court of the United States erred in finding that appellants, through their partnership, McKay and Carlen, were not engaged in the business of cutting timber for sale on their own account.

3. The Tax Court of the United States erred in finding that appellants' cedar logs were to be sold to E. K. Bishop Lumber Company only.

4. The Tax Court of the United States erred in finding that the partnership of McKay and Carlen did not have any timber for sale.

5. The Tax Court of the United States erred in finding that Neuskah Timber Company (later Bishop) did not retain title to the timber until cut and sold for security purposes.

6. The Tax Court of the United States erred in finding that the partnership of McKay and Carlen was employed to cut the timber for compensation.

7. The Tax Court of the United States erred in finding deficiencies against all appellants for the years 1947, 1948, 1949 and 1950 in lieu of a determination that there is no income tax due from appellants for any of the years in controversy, except as admitted by appellants in the Stipulation of Facts.

8. The Findings and Conclusion as set forth in the Opinion of the Tax Court of the United States pertaining to the foregoing are contrary to the evidence and in accordance with law for the following reasons:

(a) The facts found, and upon which the Court's decision is based, are not supported by substantial evidence and are contrary to the testimony of witnesses as to the ownership of the logs and the right to sell the logs cut by appellants.

(b) The Court's decision is contrary to the facts found.

(c) The Court erred in interpreting the requirements of Section 117 (k) (1) of the Internal Revenue Code.

Dated October 30, 1953.

/s/ CHARLES F. OSBORN,
Counsel for Petitioners

Proof of Service attached.

[Endorsed]: Filed October 31, 1953. Paul P. O'Brien, Clerk.

[Title of U. S. Court of Appeals and Cause.]

STIPULATION

It is hereby stipulated by and between the parties through their respective counsel that all of the exhibits in the above-entitled consolidated cases may be considered as parts of the printed record, and that the parties may refer to the exhibits in their respective briefs and oral argument.

November 13, 1953.

/s/ CHARLES F. OSBORN,
Counsel for the Petitioners.

/s/ H. BRIAN HOLLAND,
Assistant Attorney General,
Counsel for the Respondent.

[Endorsed]: Filed November 16, 1953. Paul P. O'Brien, Clerk.

[Title of U. S. Court of Appeals and Causes.]

STIPULATION REDUCING RECORD

It Is Hereby Stipulated, by and between the parties through their respective counsel, that the following cases with the Tax Court of the United States designation, which cases were consolidated for hearing before said Tax Court and are consolidated for purpose of appeal:

Helga Carlen, Petitioner, vs. Commissioner of Internal Revenue, Respondent, Tax Court Docket

No. 37662; John T. Carlen, Petitioner, vs. Commissioner of Internal Revenue, Respondent, Tax Court Docket No. 37663; Cathryn McKay, Petitioner, vs. Commissioner of Internal Revenue, Respondent, Tax Court Docket No. 37664; Arthur R. McKay, Petitioner, vs. Commissioner of Internal Revenue, Respondent, Tax Court Docket No. 37665; Arthur R. and Cathryn McKay, Petitioners, vs. Commissioner of Internal Revenue, Respondent, Tax Court Docket No. 42122; John T. and Helga Carlen, Petitioners, vs. Commissioner of Internal Revenue, Respondent, Tax Court Docket No. 42123;

present common questions which when determined will decide all of the six listed cases; that the variations in the pleadings are only as to names of petitioner, amounts involved and taxable years; that the pleadings in John T. Carlen and Helga Carlen, husband and wife, Petitioners, vs. Commissioner of Internal Revenue, Docket No. 42123, shall alone be printed as part of the printed transcript and that the pleadings in the five companion cases be considered as part of the printed record and that the parties may refer to the pleadings in their respective briefs and oral argument.

It is therefore respectfully requested that this Court permit the printing of the pleadings in John T. Carlen and Helga Carlen, husband and wife, Petitioners vs. Commissioner of Internal Revenue, Docket No. 42123, The Tax Court of The United States, as part of the printed transcript in this appeal and that the pleadings in the five companion

cases need not be printed as part of the printed transcript.

/s/ CHARLES F. OSBORN,
Counsel for Petitioners.

/s/ H. BRIAN HOLLAND,
Assistant Attorney General,
Counsel for the Respondent.

December 18, 1953.

Upon the above Stipulation It Is So Ordered.

Dated December .., 1953.

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Judge, United States Court
of Appeals.

[Endorsed]: Filed Dec. 21, 1953, Paul P. O'Brien,
Clerk.